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BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation Leased Commercial Access	MM Docket No. 92-266 CS Docket No. 96-60

COMMENTS OF TELE-COMMUNICATIONS, INC. AND
REQUEST FOR FURTHER RECONSIDERATION

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May 15, 1996

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SUMMARY

TCI urges the Commission to reject or modify many of the changes to the leased access rules at issue in this proceeding.

The Commission Should Not Require Cable Operators To Subsidize Commercial Leased Access. Section 612 of the Cable Act makes clear that commercial leased access is intended for the use of commercially viable access programmers. The Cable Act is explicit in its mandate that commercial leased access should not adversely affect the operation, financial condition or market development of cable systems. If the Commission implements the cost based leased access rate formula set out in the *NPRM*, conventional cable program services that are viable, diverse, often independent, niche-oriented and popular, will be displaced in favor of leased access users offering home shopping and infomercial programming at a heavily subsidized leased access rate. Such displacement will come at a heavy cost to the market development and financial condition of the cable operator.

The *NPRM* Rate Formula Excludes The Lost Opportunity Cost Of Programming A Cable Channel To Attract Or Retain Cable Subscribers. The Commission concludes that such loss is "too speculative." Such losses, while difficult to quantify, are extremely significant. Each channel programmed by the operator is an opportunity to attract or retain subscribers. Each channel taken away by leased access reduces that opportunity. The fundamental importance of this excluded "opportunity cost" is demonstrated by the fact that most programming services likely to be deleted as a result of leased access yield a **negative** net opportunity cost under the Commission's narrow formula.

Subscriber Surveys Establish That The Loss Of Channels Dramatically Affects Subscribers' Perceived Value Of Cable Service. TCI conducted a subscriber survey in three cable systems to probe the significance of programming changes that could ensue if the Commission's "cost formula" is implemented. The survey shows that no less than twenty-five percent of the three systems' cable subscribers would "definitely" cancel their cable service if the designated channels were to be deleted. Eighty percent of subscribers noted that loss of the channels designated for deletion in those systems would either substantially or very substantially lower the value of their cable television service. Almost eighty percent would switch to another video program distributor (such as DBS or MMDS) if the alternative distributor offered the same service at a comparable price but did not have to delete existing services to make room for leased access.

Programming Opportunity Cost Is The Most Important Cost Factor. All of the above evidence leads to the inescapable conclusion that the Commission has omitted the most important economic factor—the ability to program a channel to attract or retain subscribers—in determining whether the *NPRM*'s leased access rate formula will have an adverse effect on cable operations. It is critical that any leased access rate formula adopted by the Commission appropriately consider and compensate the cable operator for this opportunity cost.

The Commission Should Retain The Highest Implicit Fee Formula. The highest implicit fee formula has proven to be a reasonable approach to the problem of arriving at a leased access price which adequately compensates the cable operator and avoids the problem of service migration. The leased access user's payment to the cable operator is not a double payment of subscriber fees, but a reasonable surrogate for the lost value to the operator when a channel is converted to leased access programming.

Leased Access Users Have No Right To Basic Or Tier Carriage. The provisions of Section 612 do not create a right of basic or tier carriage for leased access users. However, if the Commission confers such a right, cable operators should be compensated for the value of the "free ride" access users seek from basic or expanded tier carriage.

The Commission Should Clarify Cable Operators' Right To Negotiate Below The Maximum Rate. In order to encourage cable operators to negotiate leased access rates below the maximum rate, TCI asks the Commission to affirm by rule the right of operators to negotiate rates below the maximum, based on the programming of the leased access user (as specifically allowed by Section 612(c)(2))—particularly to encourage educational, minority and local programming. The Commission should also specify that such lower rates do not establish a precedent for other potential leased access users.

Section 612 Does Not Allow The Commission To Impose Mandatory Preferential Rates For "Not-For-Profit" Users. The plain language of the Act contemplates that profit and not-for-profit entities will be treated equally and rejects any mandatory rate preference for not-for-profit entities. The Commission should be aware that many not-for-profit entities exist not to advance any public interest purpose, but simply to serve the members of their particular association.

Cable Operators Should Not Be Required To Devote New Channels To Part-Time Leased Access Until Existing Part-Time Channels Are Substantially Utilized. Because part-time carriage is extremely damaging to existing programmers, additional leased access channels should not be provided for part-time leased access applicants unless and until such applicants collectively provide at least 18 hours of programming per day per channel.

Current Leased Access Rates For Part-Time Programming Do Not Provide Reasonable Compensation. To the extent part-time carriage is required, cable operators should be allowed to increase the maximum rate by a fixed percentage (10 percent increase per hour) as the amount of the leased access time decreases below 24 hours. The resulting rates would help reduce the discrepancy with existing commercial programming rates.

Repetitive Programming Should Be Limited By Rule. The Commission should impose a limit on leased access users such that programming may not be repeated more than two times in a week, and that each month at least 50 percent of the total programming offered by the leased access user must be nonrepeat programming. Such a restriction would advance the purposes of Section 612 by promoting program diversity.

Processing Of Leased Access Applicants On A "First Come, First Served" Basis Should Not Be Mandated. Rather than the strict "first come, first served" rule proposed by the Commission, TCI suggests that cable operators should be given at least a six-month period from the time the first leased access request is received (after the effective date of the new leased access rate rules) to evaluate all leased access requests received during that period and to negotiate the various rates for such leased access users. A reasonable evaluation and negotiation period from receipt of the first request would increase the ability of operators to negotiate rates below the maximum if desirable programming is offered, and also to make reasonable decisions on leased access channel positions.

Resale Of Leased Access Time Should Not Be Required. To allow resale by leased access users will essentially read out of the statute cable operators' right to consider content in establishing rates. Allowing leased access resale will also eliminate the operator's ability to prohibit or channel obscene or indecent programming as currently required by the statute.

The Proposed Rule Changes Implicate Operators' Constitutional Rights. A leased access formula that is less than compensatory will violate cable operators' constitutional rights to due process and just compensation under the Fifth Amendment and impair cable operators' First Amendment rights.

Request For Further Reconsideration. The Commission should reconsider certain of the rule changes made in the March 29 Order:

- **The Commission Should Reconsider The Requirement That Cable Operators Lease Channel Time In Half Hour Increments**. This requirement is damaging because it encourages excessive infomercial programming and because subsidized leased access rates disrupt the existing market for these programming slots.
- **The Commission Should Reconsider Its Decision And Include All Retransmission Consent Stations In The Leased Access Set Aside Calculation.** Because federal law requires the carriage of all local commercial television stations if they request must carry, the cable operator must make channel lineup and programming decisions on the assumption that each qualified local channel will select must carry.

Thus all channel allocations for local commercial television stations are "required for use by federal law or regulation."

- **The Commission Should Reconsider Changes In Calculation Of The Highest Implicit Fee For Home Shopping Channels And Premium Channels**. The changes made by the March 29 Order could encourage migration of existing services to leased access.
- **Finally, on procedural matters,** the Commission must require leased access requests to be in writing. It should give the cable operator a reasonable time (fifteen business days) to respond to such requests and should not mandate disclosure of specifics about channel availability, other than whether at least one channel is available. The operator must have the right to require security deposits.

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COMMENTS OF TELE-COMMUNICATIONS, INC. AND
REQUEST FOR FURTHER RECONSIDERATION

Tele-Communications, Inc. ("TCI") hereby files its Comments and its Request for Further Reconsideration in the above-captioned proceeding in response to the *Order on Reconsideration of the First Report and Order ("Order") and Further Notice of Proposed Rulemaking* ("*NPRM*") released on March 29, 1996.

The Commission has signalled in this proceeding an interest in encouraging commercial leased access activity. It does not appear, however, to have fully considered the negative ramifications of a regulatory policy that understates commercial leased access costs. Congress never intended commercial leased access to harm cable operators. To the contrary, Congress mandated in the Cable Communications Policy Act of 1984[1] ("1984 Cable Act")

[1] Pub. L. No. 98-549, 98 Stat. 2779 (1984).

that leased access terms should be "at least sufficient to ensure that such use will not adversely affect the operation, financial condition, or market development of the cable system."[2] In an era of increasing competition in the multichannel video marketplace, it would be particularly inappropriate now to require cable operators to subsidize leased access users. TCI urges the Commission to abandon its proposed rate formula and fashion a regulatory scheme that properly compensates cable operators for leased access capacity.

I. MAXIMUM LEASED ACCESS RATES PROMULGATED BY THE COMMISSION SHOULD NOT REQUIRE A SUBSIDY OF LEASED ACCESS USERS BY CABLE OPERATORS.

Neither the 1984 Cable Act nor the Cable Television Consumer Protection and Competition Act of 1992[3] ("1992 Cable Act") permits, and public policy does not warrant, promulgation by the Commission of maximum leased access rates that subsidize leased access users and undercompensate cable television operators. As Section II of our comments will demonstrate, however, the *NPRM* proposes a maximum leased access rate formula which dramatically undervalues leased access channels and acts as a comprehensive subsidy for leased access use.

A. Section 612 Does Not Allow The Commission To Promote Commercial Leased Access Channel Occupancy Through Subsidized Rates.

In establishing the commercial leased access obligations, Congress was careful to limit the burden such obligations would impose on cable operators. The 1984 Cable Act ensured that operators could negotiate with potential leased access users to establish price,

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2 Communications Act, Section 612(c)(1), 47 U.S.C. § 532(c)(1) ("Section 612").

3 Pub. L. No. 102-385, 106 Stat. 1460 (1992).

terms and conditions of such use which would not be damaging to the cable system.[4] The 1992 Cable Act subsequently authorized the Commission to establish maximum leased access rates and terms, but still subjected the Commission to the specific limitation that such rates and terms not adversely affect the operation, financial condition or market development of the cable system.[5] Neither the 1984 Cable Act, which created commercial leased access, nor the 1992 Cable Act, which authorized the Commission to set maximum leased access rates and terms, allows the Commission to promote increased use of commercial leased access through subsidized leased access rates. Such a policy would be contrary to both the statutory scheme and the public interest.

B. Subsidized Leased Access Rates Are Not An Appropriate Response To Problems In The Leased Access Marketplace.

The leased access set-aside mandated under Section 612 is expressly designed for "Commercial Use." Leased access channel capacity is for commercially viable access programmers—those who can pay a compensatory rate for use of the cable operator's facilities and access to the operator's subscribers. The legislative history to the 1984 Cable Act specifies:

> The term commercial use is employed to distinguish from public access uses which are generally afforded free to the access user, whereas third party leased access envisioned by this section will result from a commercial arrangement between the cable operator and the programmer with respect to the rates, terms and conditions of the access use.[6]

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4 Section 612(c)(1).

5 Pub. L. No. 102-385, 106 Stat. 1460 § 9(c)(1) (1992).

6 H.R. REP. NO. 934, 98th Cong., 2d Sess. (1984) ("1984 House Report") at 48.

The *NPRM* appears to recognize this distinction: "We do not believe that Congress intended that cable operators subsidize programmers who seek access to their system through the provisions of Section 612."[7] But notwithstanding this recognition, the Commission struggles in the *NPRM* with whether a perceived shortfall in leased access use means that the maximum leased access rate is too high. In one part of the *NPRM*, the Commission asserts that the absence of significant leased access use requires revision of the existing "highest implicit fee" formula.[8] Later, the Commission acknowledges that "as long as the maximum leased access rate is reasonable . . . minimal use of leased access channels would not indicate that the rates should be lowered."[9] Indeed, the Commission cites to the 1984 Cable Act legislative history in which Representative Wirth, then Chairman of the House Subcommittee on Telecommunications, Consumer Protection and Finance, unambiguously stated that "an operator cannot be found to have acted in bad faith or to have established unreasonable rates simply because parties seeking access chose not to meet the offered rate."[10] The Commission also references the legislative history to the 1992 Cable Act which found that: "The cable

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[7] *NPRM* ¶ 27. The Commission has appropriately noted that "noncommercial" use of cable operators' channels has already been mandated on a substantial level. *Id.* In addition to must carry channel requirements, there has been a significant growth in the number of public educational and governmental access ("PEG") channels required in local franchises over the past several years. Entities that are not viable "commercial" users of channel capacity continue to have opportunities for expression over PEG access channels.

[8] *NPRM* ¶ 6.

[9] *NPRM* ¶ 24.

[10] 130 Cong. Rec. H10441 (daily ed. Oct. 1, 1984), (colloquy between Reps. Timothy E. Wirth and Thomas J. Bliley, Jr.).

industry has a sound argument in claiming that the economics of leased access are not conducive to its use."[11]

The "economics of leased access" are even more complex than Congress imagined. Without substantial operator discretion on leased access rates, leased access will rarely, if ever, work in favor of the small, independent programmer. As is explained in subsection C below, conventional cable programmers are dependent on sharing subscriber revenues through the affiliate fees that they charge to cable operators. Consequently, the only program services that can use leased access are those that generate significant revenues through nonsubscriber sources. Leased access, therefore, will rarely be used except by entities devoted primarily to direct sales.[12]

While leased access does not work for most conventional, commercial cable television program services, these services still enjoy ample opportunity for carriage. The national market for such program services is filled with diverse, niche-oriented services, many of them unaffiliated with any cable operator, offering professionally produced, original programming. This market is vigorously competitive and has grown exponentially in the last decade. Cable operator investment in such programming services, in the form of affiliate fees, has greatly contributed to this growth. Cable industry payments to cable programmers,

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[11] *NPRM* ¶ 26 (citing S. REP. NO. 92, 102d Cong., 1st Sess. (1991) ("1992 Senate Report") at 31-32).

[12] This is discussed in more detail in Part I(C) below. The analysis is supported by the economic report submitted by Stanley M. Besen and E. Jane Murdoch, *An Economic Analysis of the FCC's Cable Leased Access Proposal* (Charles River Associates, 1996) ("Besen/Murdoch Report") at 17. The Besen/Murdoch Report is Attachment A to these Comments. It is also supported by the Affidavit of Madison Bond ("Bond Aff.") (Attachment B) at ¶ 6.

which totalled about $1.74 billion in 1984, rose to $4.963 billion in 1995.[13] There were 48 national cable networks in 1984 and 137 in 1995.[14] Cable operators experience substantial demand from cable subscribers for some of these conventional program services.

As the next subsection of these comments demonstrates, if the Commission mandates artificially low leased access rates in order to promote commercial leased access usage, viable, diverse, niche-oriented national services, many of them newly launched, will be displaced in favor of shopping and infomercial programmers enjoying a heavily subsidized access rate. Such displacement will come at a heavy cost to the market development and financial condition of the cable operator.

C. Subsidization Of Leased Access Will Dramatically Reduce Programming Diversity.

In its *NPRM*, the Commission examined the legislative purposes of both the 1984 Cable Act's creation of Section 612 and the 1992 Cable Act's modification of that Section. It found:

> The 1992 amendments did not, however, eliminate the purposes established by the 1984 Cable Act (i.e., to promote diversity of programming sources 'in a manner consistent with growth and development of cable systems.') The Commission must therefore seek to promote competition and diversity of programming sources on the one hand, as well as to further the growth and development of cable systems on the other.[15]

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[13] National Cable Television Association, CABLE TELEVISION DEVELOPMENTS (Spring 1996) at 7.

[14] *Id.* at 6.

[15] *NPRM* ¶ 25 (footnote omitted).

In fact, any leased access rate that is designed to subsidize leased access users will both substantially harm cable operators' market development **and** significantly decrease the diversity of programming sources available to cable subscribers.

The reality of the programming marketplace is that there has been dramatic growth in both affiliated and unaffiliated cable programming services since the passage of the 1984 Cable Act, and particularly since passage of the 1992 Cable Act. We have attached a list of **unaffiliated** cable programming services drawn from the Commission's *Second Annual Report to Congress Concerning the Status of Competition in the Market for the Delivery of Video Programming*[16] and updated by recent trade press reports,[17] which shows 227 regional and national cable program services in operation, approximately 113 of which are unaffiliated with any cable operator. More than 100 additional services are in the planning stages, with approximately 89 of these channels unaffiliated with any cable operator.[18] Diverse program services from both affiliated and unaffiliated programming sources continue to pour into the marketplace—all without the benefit of subsidized leased access rates. That such program services are gaining access to cable television systems can be demonstrated by TCI's own experience. TCI recently concluded plant upgrades for systems in McKeesport, Pennsylvania;

[16] Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming, *Second Annual Report*, CS Docket 95-61, FCC 95-491 (rel. Dec. 11, 1995).

[17] *New Network Handbook*, CABLEVISION, Apr. 29, 1996 (supplement); *Aspiring Networks—The Latest List*, MULTICHANNEL NEWS, Apr. 29, 1996, at 82.

[18] *See* Part I, Unaffiliated Program Services Already Launched and Part 2, Unaffiliated Program Services To Be Launched (Attachment D). While it is sometimes difficult to determine from public sources all entities with an ownership interest, these entities have been determined, with reasonable certainty, to be unaffiliated with any cable operator.

Garland and Euless, Texas; and Olympia, Washington, which resulted in the following services being added to one or more of these systems: Faith and Values, The Learning Channel, ESPN II, The Cartoon Network, The Box, Home and Garden, Mind Extension University, The History Channel, The Sci-Fi Channel, C-SPAN II, E!, Court TV, TV Food Network, The Travel Channel, Cable Health Club, Black Entertainment Television, Univision, Country Music Television, The Nashville Network, GEMS, and local news channels. As of June 1, 1996, TCI will launch The Sci-Fi Channel in systems representing nearly 2 million subscribers.

To measure the effect of the *NPRM*'s proposed leased access rate formula on program carriage, TCI applied the Commission's proposed cost/market formula to six representative cable systems. The *NPRM* formula initially requires designation of the particular services which would be deleted to accommodate leased access programming.[19] The list of services that TCI tentatively concludes would be deleted from the Denver, Colorado; Washington, D.C.; Chicago, Illinois; Tulsa, Oklahoma; Houston, Texas and Seattle, Washington cable systems is provided at Attachment E. The number of channels to be deleted on each system ranges from 4 to 9, depending on the system's current channel capacity. Many of the services at issue are unaffiliated with any cable operator. The services tentatively designated for deletion include:

[19] *NPRM* ¶ 76.

C-SPAN	The Comedy Channel
CNBC	Court TV
ESPN 2	The Weather Channel
Arts & Entertainment Network	Discovery Channel
Bravo	VH-1
American Movie Classics	The Learning Channel
Faith & Values	fX
CNN-Headline News	Lifetime Television

Each of these programming services represents a diverse programming service valued by cable subscribers, often a "niche" service. Therefore, the practical result of any Commission leased access rate that subsidizes leased access users to promote increased leased access use would be a deletion of affiliated and non-affiliated programming sources which unquestionably add diversity to the channel line-up.

The obvious question is what diversity, if any, will subscribers gain through commercial leased access. The economics of cable programming suggest that the vast majority of such users will offer home shopping and infomercials. Most conventional cable program services cannot and do not lease channels from cable operators, because they depend for a significant portion of their revenue on the affiliate fees they charge to cable operators; but home shopping services and infomercial providers can and do use leased access because their production costs are relatively low and their sales programming provides direct income without the need to rely on affiliate fees. As explained by Stanley Besen and Jane Murdoch in their economic analysis,

> [M]ost incumbent program services depend for a significant portion of their support on being able to share in direct subscriber payments through the affiliate fees they charge to cable operators. For example, American Movie Classics, which obtains no advertising revenues, depends entirely on its share of basic subscriber revenues. Even a service like MTV generates about one-quarter of its revenues through affiliate fees. An

> existing subscriber-based program service cannot bid to be a leased access programmer because, by definition, it needs subscriber revenues to survive. Similarly, among new services, those that are dependent on subscriber revenues will be unable to bid for leased access channels.
>
> The only services that *can* pay significant explicit access charges are those that generate significant revenues through nonsubscriber sources. Certain types of programmers, especially home-shopping services and suppliers of infomercials, enjoy an advantage in the competition for leased access channels because none of their revenues are the result of subscriber fees.[20]

This conclusion is supported by the statement of Madison Bond, a Vice President of TCI's programming subsidiary:

> The majority of entertainment-based, ad-supported cable networks depend over the long term on a dual revenue stream of license fees and advertising revenue. In most cases, the only services that pay for carriage on a cable system are home shopping services, infomercial services, gambling services, and other services with a transactional or promotional component to their programming. It may be anticipated that if leased access rates are substantially reduced, home shopping services, infomercial services, and gambling services will predominate in the leased access category.[21]

Further support for the conclusion that leased access users are mostly those who have something to sell comes from Deborah Friday, General Manager of TCI Media Services, Inc. for Denver operations, who observes that,

> Most leased access requests that we receive are for infomercial programming. Generally, leased access applicants have something to sell and seek to use leased access for that purpose. For instance, we have an active lease with a local auto

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[20] Besen/Murdoch Report (Attachment A) at 16-17 (emphasis in original).

[21] Bond Aff. (Attachment B) at ¶ 6.

> dealership which uses leased access for a half hour automotive infomercial. We have other leased access applications pending for automotive and real estate infomercials."[22]

Given the likely nature of leased access programming, subscribers would suffer a dramatic loss in program diversity if the Commission, even inadvertently, establishes a rate that subsidizes the carriage of commercial leased access users.

A Commission rate designed to promote increased leased access use would not only require the deletion of existing programming services, but would perhaps fatally preclude the addition of developing programming services. For example, the History Channel (unaffiliated with any cable operator) has been listed as the service most likely to be added in the next year by all cable operators.[23] Services such as Kaleidoscope (for physically challenged individuals), BET on Jazz, the Sci-Fi Channel and GEMS (Hispanic programming) also would be stymied in their attempts to gain channel access. The channel capacity that might otherwise accommodate these services would be forfeited to subsidized leased access users for home shopping and infomercial channels.

Any Commission leased access rate which, even unintentionally, subsidizes leased access users at the expense of existing programming services and cable operators could result in a dramatic loss of diverse programming. Over 63 million cable households would be deprived of significant educational, cultural and minority programming services and would, in their place, receive multiple channels of home shopping and infomercials. Such a result fundamentally undermines the purposes of Section 612, which the Commission found to be to

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[22] Affidavit of Deborah Friday ("Friday Aff.") (Attachment C) ¶ 2.

[23] Rich Brown, *History Has Cable Future*, BROADCASTING & CABLE, Apr. 22, 1996, at 47.

"promote competition and diversity of programming sources on the one hand, as well as to further the growth and development of cable systems on the other."[24]

II. THE COMMISSION'S PROPOSED LEASED ACCESS "COST FORMULA" IS FUNDAMENTALLY FLAWED.

A. The Commission's Proposed Formula Neglects To Value The Most Important "Opportunity Cost."

The Commission proposes a leased access rate formula based upon the "net opportunity costs" that a cable operator incurs by leasing a channel.[25] The Commission compares the operator's current channel usage with its leased access usage. It essentially limits the "net opportunity costs" to advertising revenues or shopping commissions the cable operator would forego—offset against the licensing fees the operator would save.[26] The Commission's "opportunity cost" formula fails to attribute **any** value to TCI's most important asset—the ability to program a cable channel for its highest value use. The Commission's formula fails to consider the value of operator-selected programming in retaining or adding cable subscribers. It assumes that all programming is equal in the eyes of the customer and that the customer will be equally happy receiving leased access home shopping and the Discovery Channel.

In adopting the formula with this critical omission, the Commission stated:

> We tentatively conclude that the cost formula should not explicitly include revenue lost because of a purported loss in subscribership to a particular tier because particular programming is dropped. We tentatively conclude that, in the

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[24] *NPRM* ¶ 25.

[25] *NPRM* ¶ 79.

[26] *NPRM* ¶¶ 80, 81, 82 and 83.

> tier context, any such subscriber loss is too speculative to measure accurately.[27]

The basic assumption underlying the Commission's proposed approach—that subscribers don't care what they watch and that subscriber revenues will be unaffected if existing program services are removed to make room on the basic service or cable program service tiers for leased access programming—is false. Economists Besen and Murdoch observe:

> Subscriber revenues would undoubtedly be affected adversely if this were to occur. . . . [I]t may be exceedingly difficult to measure these revenue losses, or opportunity costs . . . in part, because the revenues generated by one program service depend on how many and which other services are also being offered.[28]

When subsidized leased access is substituted for existing programming, the cable operator's consequential losses of subscribers and subscriber fees may be difficult to quantify, but they nonetheless are extremely significant. As explained in the Affidavit of Camille Jayne, a Senior Vice President of a TCI affiliate with responsibility for strategic business development, the ability to attract additional cable subscribers and build subscriber loyalty is dependent upon offering the appropriate mix of diverse and niche programming services.

> Having the right product, tiers and packages is a key element that will enable us to compete and survive in today's and tomorrow's increasingly competitive marketplace. Loss of programming control will significantly impact penetration and revenues. The investment we make in advertising, plant, equipment and new technologies will only be well spent if we

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[27] *NPRM* ¶ 86.

[28] Besen/Murdoch Report (Attachment A) at 13-14.

> have the right mix of content that appeals to very specific segments, which in turn will motivate them to buy our service.[29]

Each channel, therefore, represents an opportunity for the cable operator to retain or add cable subscribers. Each channel taken away by subsidized leased access reduces that opportunity.

The use of program packaging to retain or add subscribers is not only a tool for market development, it is the primary and essential tool. By excluding the cable operator's most important opportunity cost—the lost ability to retain or attract cable subscribers through programming the system's channels—the proposed leased access formula abrogates the Commission's statutory responsibility to ensure that any leased access rate "not adversely affect the operation, financial condition, or market development of the cable system."

B. *NPRM* Cost Formula Calculations Based On Real Systems Yield Negative Access Rates.

The Commission's basic analytical flaw is underscored by the leased access rate produced by the Commission's formula. In order to evaluate the leased access rate produced by the Commission's opportunity cost formula, TCI applied the formula to the six previously identified TCI cable systems. As shown on Attachment E, application of the Commission's proposed opportunity cost formula results in each of the six systems having a **negative** leased access channel rate. For every system, the licensing fees saved by the cable operator were significantly greater than the advertising revenues or sales commissions generated by the services to be replaced by leased access users. The highest rate calculated was for the Chicago cable system, with a monthly leased access rate of negative $.03 per subscriber per

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[29] Affidavit of Camille Jayne ("Jayne Aff.") (Attachment F) ¶ 4.

channel. Application of the formula to the Seattle system resulted in a monthly leased access rate of almost negative $.10 per subscriber per channel. Under the Commissions economic theory, a cable operator should not even be carrying these services, as it is detrimental to do so.

A leased access formula that yields a negative rate is obviously excluding a significant opportunity cost. The Commission has, in fact, specifically identified that missing component: "We suspect that, if a channel has a negative opportunity cost, it may be because the cost formula does not include an approximation of the value of subscriber penetration."[30] The Commission's observation could not be more on point. Of the 47 existing programming services designated for deletion on the six TCI systems, 38 (81%) had a negative net opportunity cost under the Commission's formula. There could not exist clearer evidence that the vast majority of channels that would be deleted pursuant to a reduced leased access rate are carried solely for the purpose of retaining or adding cable subscribers. Thus, the Commission's opportunity cost formula has omitted by far the most important opportunity cost factor. If TCI did not believe these 38 services would help to retain or attract new subscribers on the six systems, the Commission's "negative opportunity cost" assessment would argue for their immediate deletion.

The Besen/Murdoch Report also has analyzed the Commission's proposed opportunity cost formula and has concluded that it is fundamentally flawed. According to the Report, many of the flaws in the Commission's proposed approach stem from an erroneous view of the nature of the service that cable operators offer to their subscribers:

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[30] *NPRM* ¶ 88.